States Vs. Uncle Sam: Federal Bonds As Unclaimed Property

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Law360, New York (September 5, 2017, 12:02 PM EDT) -- States are continuing to assert claims against the federal government over unredeemed federal savings bonds under their respective unclaimed property statutes. Billions of dollars are at stake, and nine states have brought lawsuits against the federal government in the U.S. Court of Federal Claims to redeem bonds whose owners’ last known addresses are in their states. In an opinion issued in 2015 and two opinions issued on Aug. 8, 2017, the Court of Federal Claims held that state unclaimed property statutes are not preempted by federal law and the federal government is required to recognize states’ ownership claims to the bonds based on state escheat judgments.[1] In addition to being a step toward a huge windfall for the states, these decisions are noteworthy because they potentially conflict with decisions of the U.S. Court of Appeals for the Third Circuit and the U.S. District Court for the District of Columbia.[2]

All 50 states have statutes governing the disposition of unclaimed property, which is tangible or intangible property that has been lost or abandoned by its rightful owner for a statutorily determined period of time. The legal framework for the ongoing savings bond disputes was established in a 2012 Third Circuit decision denying New Jersey and other states’ claims against the federal government. In Treasurer of New Jersey v. U.S. Department of the Treasury, 684 F.3d 382 (3d. Cir. 2012), the Third Circuit held that the Treasury’s regulations — providing that payment on federal savings bonds would be made only to the registered owner unless a third party obtained ownership through valid judicial proceedings — preempted the state unclaimed property statutes. The Third Circuit noted that Congress had authorized the Treasury to implement regulations allowing savings bonds to be kept until after maturity to make them “attractive to savers and investors.” In contrast, the state statutes specified that the bonds become unclaimed property over which the states may take custody if not redeemed within a time period as short as one year after maturity. According to the Third Circuit, the states’ unclaimed property statutes interfered with the bond contracts’ incorporation of federal regulations because they made the states, rather than the federal government, the obligor on the bonds. Applying the principle of intergovernmental immunity, the Third Circuit also determined that the states’ unclaimed property statutes would unlawfully
regulate the federal government by requiring it to comply with state accounting, record-keeping and reporting requirements.

After the U.S. Supreme Court denied the states’ petition to appeal the Third Circuit’s decision, many states began acquiring escheat judgments to establish bond ownership through “valid, judicial proceedings.”[3] In 2013, Kansas brought a lawsuit against the federal government in the Court of Federal Claims to recover bond proceeds based on an escheat judgment. After the case was filed, however, the Treasury amended its regulations in 2015 to state that it would not recognize the transfer of bond ownership through escheat judgments.[4]

Five states challenged the Treasury’s new rule as arbitrary and capricious under the Administrative Procedure Act in the U.S. District Court for the District of Columbia.[5] In Estes v. U.S. Department of the Treasury (Estes I), 219 F. Supp. 3d 17 (D.D.C. 2016), the district court found in favor of the federal government, concluding that the revised regulation was not inconsistent with any clearly established prior policy, but even if it was, the Treasury had not violated the APA because it did not “depart from [its] prior policy sub silentio or simply disregard rules that are still on the books.”[6] The district court noted that the Treasury had “extensively explained its [r]ule and its view as to why that [r]ule did not contradict prior statements,” and there was thus “no basis for concluding that [the Treasury] casually ignored prior policies and interpretations or otherwise failed to provide a reasoned explanation for its [rule].”[7]

Recent decisions in the Court of Federal Claims, however, appear to have breathed new life into the states’ claims. In the cases before the Court of Federal Claims, Judge Elaine Kaplan has been critical of the Treasury’s “ever-shifting explanations for denying states’ requests to redeem absent bonds,” even comparing it to a game of “whack-a-mole.”[8] Because these cases involve state court escheat judgments obtained before the Treasury’s revision of its regulation, the court did not apply the provision explicitly excluding “[e]scheat proceedings” from the kinds of “valid, judicial proceedings” that can transfer ownership of federal savings bonds.[9]

In Estes II, the Court of Federal Claims held that the state had the more persuasive reading of the regulatory text and concluded that the Treasury’s litigating position was not entitled to any deference because it conflicted with 60 years of interpretive guidance, statements on its website, and positions taken in prior litigation. And, in LaTurner and Lea, the court held that the state unclaimed property statutes, which presumed bonds abandoned five years after their maturity date, were not preempted by the Treasury’s regulations because there was no conflict. The court stated that the Treasury’s regulations themselves put bond owners on notice that the right to hold onto the bond after it matures is not unlimited. The court also noted that, once ownership is transferred to the state under the Treasury regulations, the state would need to follow the existing federal regulations — not state procedures — to redeem the bonds. Similarly, the principle of intergovernmental immunity did not apply because the Treasury regulation (as interpreted by the court) granted title to the state, meaning that federal property was no longer at issue.

Judge Kaplan distinguished the Third Circuit decision primarily on the ground that it dealt with custody-based, rather than title-based, unclaimed property statutes. She stated that the same concerns about double liability or interference with federal procedures did not exist because, in taking title to the bonds, the state would merely step into the shoes of the prior owner vis-à-vis the federal government.

Judge Kaplan also subtly acknowledged the possible conflict between her interpretation of the Treasury regulation and the district court’s reasoning in Estes I, but maintained that the courts were reviewing different issues under different standards. There is, however, no dispute that the revised regulation will govern future claims by states. This means that, while states that obtained escheat judgments before the
revision can continue to pursue claims for hundreds of millions of dollars or more, other states may not have the same success. The appeal of Estes I is currently pending before the U.S. Court of Appeals for the D.C. Circuit.[10]

The unredeemed savings bond litigation is just one example of the ongoing disputes arising out of state unclaimed property statutes. More than 25 states are now involved in a case before the U.S. Supreme Court over the right to take custody of hundreds of millions of dollars in unclaimed money orders issued in the form of official checks. Emboldened by the Court of Federal Claims’ decisions in the savings bond cases, states may no longer see federal preemption as an obstacle to claiming other kinds of assets, such as employee benefits. Meanwhile, states are continuing to pursue expansive unclaimed property audits of businesses across a wide spectrum of industries. States commonly hire contingency-fee auditors who take aggressive positions on the scope of state laws, and companies have been pushing back against unfair audit techniques in litigation pending across the country. These disputes are expected to continue as state governments aim to take custody of potentially billions of dollars in abandoned assets from numerous sources in an effort to plug state budget gaps.

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[3] 31 C.F.R. § 315.20(b)

[4] 31 C.F.R. § 315.20(b) (adding “Escheat proceedings will not be recognized under this subpart.”)


[6] Id. at 33 (citation omitted).

[7] Id.


[9] 31 C.F.R. § 315.20(b)